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SIPDIS

STATE FOR INL, EB/ESC/TFS AND WHA/CAN
JUSTICE FOR OIA AND AFMLS
TREASURY FOR FINCEN

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SUBJECT: CANADA: 2005-2006 INTERNATIONAL NARCOTICS CONTROL
STRATEGY REPORT (INCSR) PART II: FINANCIAL CRIMES AND MONEY
LAUNDERING

REF: (A) OTTAWA 3636 (INCSR PART I)

(B) STATE 210324

1. Canada is strengthening measures to reduce its vulnerability to money laundering and terrorist financing. Financial institutions remain susceptible to transactions involving international narcotics proceeds, including significant amounts of funds in U.S. currency derived from illegal drug sales in the United States. The long U.S.-Canada border and closely integrated financial sector make Canada attractive to criminals interested in cross-border crime. With over \$1 billion a day in legitimate bilateral trade, both the U.S. and Canadian governments are particularly concerned about the criminal abuse of cross-border movements of currency. Canada has no offshore financial centers or free trade zones.

Laws and Regulation to Prevent Money Laundering

2. Canada's financial intelligence unit (FIU), the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC), was created under the Proceeds of Crime (Money Laundering) Act in 2000 and started accepting Suspicious Transaction Reports (STRs) in November, 2001. The Act was amended in December 2001 to become the Proceeds of Crime (Money Laundering) and Terrorist Financing Act (PCMLTF Act). FINTRAC is an independent agency under the authority of the Minister of Finance and acts at arm's length from the law enforcement and other agencies that receive its disclosures. FINTRAC and regulators such as the Office of the Supervisor of Financial Institutions (OSFI) oversee compliance with anti-money laundering and anti-terrorist finance regimes.

3. The PCMLTF Act creates a mandatory reporting system for suspicious financial transactions, large cash transactions, large international electronic funds transfers and cross-border movements of currency and monetary instruments of C\$10,000 (about US\$8,500) or greater. Failure to report cross-border movements of currency and monetary instruments could result in seizure of funds or penalties ranging from C\$250 to C\$5,000 (about US\$200 to US\$4,000). In addition to receiving suspicious transaction reports, FINTRAC collects financial intelligence from other sources on suspected cases of money laundering, terrorist financing or threats to the security of Canada. The list of predicate money laundering offenses was expanded and now covers all indictable offenses, including terrorism and the trafficking of persons.

4. Detection of financial crime is improving as FINTRAC gains experience and compiles data. FINTRAC does not perform criminal investigations, but analyzes data and discloses suspicious cases to Canadian law enforcement, intelligence, other regulators and foreign FIUs. FINTRAC has signed 20 memoranda of understanding with foreign FIUs (including FINCEN), 13 of them in the past year. Others are being negotiated.

Financial Intelligence Unit/Investigations

5. In 2004-05, FINTRAC made 142 case disclosures, of which 110 were for suspected money laundering, 24 were for suspected terrorist financing and/or threats to the security of Canada, and 8 involved both. Of the total disclosed, 115 were new cases while 27 were follow-ups to disclosures made previously. The total dollar value of the disclosures was just over C\$2 billion (about US\$1.7 billion), almost triple the value last year. FINTRAC has not disclosed the number of STRs that were filed in 2003-04, but has compiled data on over 23 million transaction records since commencing business in 2001. FINTRAC's case disclosures have not yet resulted in prosecutions.

6. Most financial crime investigations in Canada involve narcotics proceeds, although other crimes, such as tobacco smuggling and prostitution, are associated with the unlawful movement of financial instruments. A Canadian law enforcement official notes that the prevalence of narcotics-related cases is due in part to the fact that investigations

focus on narcotics. The growth in Chinese and Colombian criminal organizations is being reflected in increased narcotics-related crime and higher levels of seizures.

Financial Sector

17. The banking and financial community cooperates with enforcement efforts to trace funds and freeze bank accounts and supports efforts to strengthen anti-money laundering and anti-terrorist financing regimes. Charities are regulated by Revenue Canada under the Income Tax Act. Financial transactions involving charities are subject to the same reporting requirements as other financial transactions.

18. Money laundering is a criminal offense, regardless of the source of the funds or size of the transaction. Financial institutions are required to know, record, and report the identity of customers engaging in significant transactions, including all cash transactions over C\$10,000 (about US\$8,500). Financial institutions must file STRs and/or be able to produce other records for FINTRAC within 30 days of request. Financial institutions must maintain account records for five years starting from the closing of the account; the last transaction; or the date of creation of the document (depending on the type of record). FINTRAC must maintain records of STRs for at least five years, with an eight-year minimum in some cases.

19. Reporting requirements apply to a wide range of entities including banks and credit unions; life insurance companies; brokers and agents; securities dealers; portfolio managers; provincially-authorized investment counsellors; foreign exchange dealers; money services businesses (including alternative remittance systems such as Hawala); crown agents accepting deposit liabilities and/or selling money orders; accountants and accounting firms; real estate brokers or sales representatives in certain client-related activities; casinos (except for some temporary charity casinos); and individuals transporting large sums across borders.

110. Reporting entities must also report the existence of terrorist property in their possession or control, or information about a transaction or proposed transaction in respect to such property. All cash transactions over C\$10,000 (about US\$8,500), as well as international electronic funds transfers and cross-border movement of currency or monetary instruments must also be reported. Failure to file a suspicious transaction report could lead to up to five years' imprisonment, a fine of C\$2,000,000, or both.

111. The Canadian government is negotiating with the Canadian bar association on ways to include lawyers under the reporting regime, and is exploring a regulatory oversight system for money services businesses (MSBs). Although MSBs legally must report suspicious or large-value transactions to FINTRAC, there is currently no regulatory system to ensure that they comply. Reporting individuals have immunity from civil or criminal prosecution for reports filed in good faith. Information that identifies reporting individuals cannot be disclosed except as specified in legislation. Information can, however, be released in limited circumstances such as parliamentary or legal proceedings. FINTRAC is not subject to search warrants.

112. In a November 2004 report to Parliament, Canada's Auditor General stated that "privacy concerns restrict FINTRAC's ability to disclose intelligence to the Police, and as a result, law enforcement and security agencies usually find that the information they receive is too limited to justify launching investigations." Parliamentary reviews of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act and the Anti-Terrorism Act scheduled for 2006 should address these issues.

Cash Smuggling

113. U.S. law enforcement officials have echoed concerns that strict Canadian privacy laws and the high standard of proof required by Canadian courts inhibit the full sharing of timely and meaningful intelligence on suspicious financial transactions. Such intelligence may be critical to investigating and prosecuting international terrorist financing or major money laundering investigations.

114. International transport of large values of currency or monetary instruments must be reported. In the case of currency or monetary instruments transported by courier or mail, the exporter or importer in Canada is responsible for filing the report. Currency and monetary instruments that are not reported appropriately are subject to forfeiture.

115. Cash smuggling reports are sent to FINTRAC, law enforcement, intelligence, customs, tax, and immigration

officials as appropriate. Records for all cash transactions amounting to \$3000 or more must be kept for five years. Last year's concern about the inability of U.S. and Canadian law enforcement officers to exchange promptly information concerning suspect funds found in the possession of individuals attempting to cross the U.S.-Canadian border has been addressed by a 2005 Memorandum of Understanding on exchange of Currency and Monetary Instrument Report data. Although this should expand the extremely narrow disclosure policy and provide a provision for sharing financial information akin to the Customs Mutual Assistance Agreement, more work needs to be done.

¶16. The Royal Canadian Mounted Police (RCMP) and Canadian Security Intelligence Service (CSIS) are responsible for investigating cases of money laundering and financial crime. Canada has the police powers and resources to trace, freeze and require the forfeit of assets.

¶17. All asset forfeiture proceedings in Canada are overseen by the Department of Justice Canada, with seized assets going to the General Fund. Canada has provisions for asset sharing with other governments involved in joint investigations, and exercises them regularly. However, there is no provision that allows for the placement of seized assets into specific law enforcement channels (such as the Treasury forfeiture fund in the U.S.).

¶18. Until November 2005, the Canadian Criminal Code provided for the forfeiture of proceeds of crime only upon application by the Crown after a conviction for an indictable offense. A new "Proceeds of Crime" program (not to be confused with the Proceeds of Crime (Money Laundering) and Terrorist Financing Act) amends the Criminal Code, the Controlled Drugs and Substances Act, the Customs Act, the Excise Act, the Proceeds of Crime (Money Laundering) and Terrorist Financing Act, and the Seized Property Management Act. The new amendments make the following changes to facilitate asset forfeiture:

-- once an offender has been convicted of either a criminal organization offense, or certain offenses under the Controlled Drugs and Substances Act, the court is directed to order the forfeiture of property of the offender identified by the Crown unless the offender proves (reverse onus) on a balance of probabilities, that the property is not the proceeds of crime;

-- in order for the reverse onus to apply, the Crown would first be required to prove, on a balance of probabilities, either that the offender engaged in a pattern of criminal activity for the purpose of receiving material benefit or that the legitimate income of the offender cannot reasonably account for all of the offender's property;

¶19. The new amendments apply to all criminal organization offenses where the offense is punishable by five or more years of imprisonment or after conviction, on indictment, for offenses under the Controlled Drugs and Substances Act (trafficking, importing, exporting, and production of drugs).

¶20. However, the legislative amendments do not contain "structuring" provisions. Therefore, although criminal proceeds can be seized, the structured deposit of funds in amounts just below the reporting requirement is not subject to prosecution under current money laundering provisions.

Terrorist Financing

¶21. The 2001 Anti-Terrorism Act created measures to identify, deter, disable and prosecute those engaged in terrorist activities or those who support these activities. The legislation makes it an offense to knowingly support terrorist organizations, whether through overt violence or through material support. The Anti-Terrorism Act requires the publication of a list of groups deemed to constitute a threat to the security of Canada and to Canadians.

¶22. Names of designated individuals and entities are circulated by the Office of the Supervisor of Financial Institutions to all regulated financial institutions. Assets of designated entities or individuals that are frozen under provisions of the Anti-Terrorism Act or UN resolutions cannot be seized by the Canadian government. The Anti-Terrorism Act is scheduled for review in 2006 to ensure consistent compliance with international standards and proposals in the Auditor General's report mentioned above.

International Cooperation

¶23. There is a web of longstanding agreements with the United States on law enforcement cooperation, including treaties on extradition and mutual legal assistance (MLAT); MOUs such as those with customs and FIUs described above; and Ministerial Directives. Canada has provisions for asset sharing, and exercises them regularly.

124. The U.S. and Canada work together closely in fighting narcotics and financial crime. Following are a sample of successful cases in 2005:

Case A: In July 2005, U.S. and Canadian officials shut down a 120-yard tunnel from British Columbia to Washington state that was intended to transport marijuana into the U.S. Three Canadians were arrested, and the tunnel was destroyed to prevent its use for other crime.

Case B: In August, 2005, police in Alberta made the largest Ecstasy bust in the province's history and seized US\$3.7 million worth of street drugs including 213,000 tablets of MDMA/Ecstasy laced with methamphetamine. This followed a seven-month RCMP drug and organized crime investigation that saw 35 people arrested in February in Edmonton for trafficking in a controlled substance, possession of a controlled substance, possession of the proceeds of crime, and firearms offenses.

Case C: Operation Sweet Tooth, a 24-month investigation that targeted international MDMA/Ecstasy and marijuana trafficking rings whose drug smuggling and money laundering operations ranged from the Far East to Canada and the U.S., resulted in the arrest of 291 individuals and the execution of 98 search warrants in both the U.S. and Canada. The seizures totaled 931,300 MDMA tablets; 1,777 pounds of marijuana; and \$7.75 million in U.S. assets. DEA, with assistance from the RCMP and the Canada Border Services Agency, dismantled two major drug transportation rings with ties to 61 separate domestic investigations. The Operation Sweet Tooth organizations were responsible for distributing 1.5 million tablets of MDMA per month. The drug trafficking syndicates laundered millions of dollars in drug proceeds through the use of bulk courier transport, money remitters and the Vietnamese underground banking system.

125. Canada is a leader in international efforts to combat financial crime, adheres to international money laundering standards, and was instrumental in drafting the FATF (Financial Action Task Force's) 40 points on money laundering. In July 2006, Canada assumes the chair of the Financial Action Task Force (FATF).

126. It is a member of the Egmont Group and the OAS Inter-American Drug Abuse Control Commission Experts Group to Control Money Laundering (OAS/CICAD). Canada also participates with the Caribbean Financial Action Task Force (CFATF) as a Cooperating and Supporting Nation, and as an observer jurisdiction to the Asia/Pacific Group on Money Laundering (APG). Canada is a party to the OAS Inter-American Convention on Mutual Assistance in Criminal Matters.

127. Canada has signed and ratified all 12 United Nations Conventions pertaining to terrorism and has listed all terrorist entities designated by the UN. Canada is a party to the UN International Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (Vienna Convention), the 1988 UN Drug Convention, the UN International Convention for the Suppression of the Financing of Terrorism, and the UN Convention Against Transnational Organized Crime. It signed the UN Convention Against Corruption in May, 2004, but has not yet ratified it.

128. The Canadian government is constantly evaluating ways in which to strengthen its anti-money laundering and anti-terrorist financing regime, working with the Egmont Group, the Financial Action Task Force and in other international fora to develop best practices. As part of this process the government is evaluating the need to expand the reach of anti-money laundering and anti-terrorist financing reporting requirements (to include, for example, the legal profession and prohibitions on "structured" deposits). Parliamentary review in 2006 of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act and of the Anti-Terrorism Act should further improve the Canadian government's ability to fight financial crime.

Links to legislation and regulations

November, 2005 amendments to the Criminal Code and the Controlled Drugs and Substances Act
<http://www.parl.gc.ca/LEGISINFO/index.asp?Lang=E&Chamber=C&StartList=2&EndList=200&Session=13&Type=0&Scope=I&query=4506&List=toc-1>

Highlights of the November, 2005 amendments:

http://canada.justice.gc.ca/en/news/nr/2005/doc_31540.html

2001 Anti-Terrorism Act

<http://laws.justice.gc.ca/en/A-11.7/index.htm> 1

2001 UN Suppression of Terrorism Regulations
<http://laws.justice.gc.ca/en/u-2/sor-2001-360/186571.html>

2000 Proceeds of Crime (Money Laundering) and Terrorist
Financing Act
<http://laws.justice.gc.ca/en/P-24.501/index.htm>

OSFI list of designated entities and individuals (terrorist
financing)
http://www.osfi-bsif.gc.ca/osfi/index_e.aspx?DetailID=525

1985 Criminal Code
<http://laws.justice.gc.ca/en/C-46/index.html>

1985 Income Tax Act
<http://laws.justice.gc.ca/en/I-3.3/index.html>

1982 Charter of Rights and Freedoms
<http://laws.justice.gc.ca/en/charter/index.htm#libertes>

WILKINS